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UNCLAS SECTION 01 OF 04 SHANGHAI 000053

SENSITIVE
SIPDIS

STATE FOR EAP/CM - WKLEIN AND SFLATT, EEB/IPE - TMCOWAN AND INL
- JVGIL
USTR FOR CHINA OFFICE - KALVAREZ, AWINTER, TWINELAND, SMCCOY,
TPOSNER, CREADE
DOC FOR NATIONAL COORDINATOR FOR IPR ENFORCEMENT - WPAUGH
DOC FOR ITA/MAC: ESZYMANSKI, JYOUNG
LOC/ COPYRIGHT OFFICE - STEPP
USPTO FOR INT'L AFFAIRS - LBOLAND, EWU
DOJ FOR CCIPS - TNEWBY
FBI FOR LBRYANT
DHS/ICE FOR IPR CENTER - DFAULCONER, TRANDAZZO
DHS/CBP FOR IPR RIGHTS BRANCH - GMACRAY, PPIZZECK
TREASURY FOR OASIA - DOHNER/WINSHIP
NSC FOR LOI

E.O. 12958: N/A

TAGS: [KIPR](#) [ECON](#) [ETRD](#) [PGOV](#) [CH](#)

SUBJECT: 2010 SHANGHAI IPR ROUNDTABLE -- CANDID COMMENTARY FROM
INDUSTRY

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¶1. (U) This cable contains business proprietary information and
is Sensitive but Unclassified. Please handle accordingly.

¶2. (SBU) Summary: Shanghai remains the "best place overall" for
IPR protection and enforcement in China despite continued
problems, according to U.S. industry representatives at a recent
Consulate-hosted roundtable. Many companies have adopted
pragmatic business strategies that allow their companies to
flourish in spite of the shortcomings in the regulatory
environment. Participants welcomed future IPR initiatives by
the USG, especially in seeking ways to convince Chinese
authorities that robust enforcement of intellectual property
protection serves China's long-term interests. End Summary.

¶3. (SBU) During a February 4 IPR roundtable hosted by ConGen
Shanghai, representatives from over 25 U.S.-based companies
discussed recent developments and continuing challenges in
protecting intellectual property rights in East China. USG
participants included Consul General Beatrice Camp; Deputy
Assistant USTR and Chief Negotiator for IPR, Kira Alvarez;
Embassy Beijing Minister Counselor for Trade, Chris Adams;
Embassy Beijing Economics Minister Counselor, Bill Weinstein;
U.S. Patent and Trademark Attachi, Nancy Kremers, Embassy
Beijing Resident Legal Advisor, Amy Lee; Embassy Beijing
Immigration and Customs Enforcement Attachi, Bruce Gordon;
Embassy Beijing Commercial Section Trade Policy Officer, Lisa
Rigoli; and Embassy Beijing Economic Officer Sally Behrhorst.

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¶4. (SBU) Several roundtable participants described how they had adopted pragmatic business practices to protect their intellectual property, including selective investment policies, allowing many of their businesses to prosper despite China's regulatory shortcomings. General Motors General Counsel Kenneth Wong noted, in order to protect core IPR, many U.S. manufacturers, including GM, only licensed the production of non-critical components to local Chinese partners allowing GM to retain the design and production of core technology in the United States. Tao Taodi of Cisco Systems stated that while this approach may have worked well in the past, the Chinese government now has its sights set on obtaining core technology and was no longer satisfied with attracting low-tech production. Tao cited tax incentives and other preferential policies such as Beijing's 2008 "High-End New Enterprise Certification," designed to attract high-tech investment as examples. (Note: The High-End New Technology Enterprise Certification reduces the corporate income tax rate from 25 percent to 15 percent. End Note).

¶5. (SBU) Roundtable participants were skeptical of the effectiveness of these incentives. Several industry representatives, particularly those from the pharmaceutical industry, expressed concern that their IP remains vulnerable to theft in China and that none of the incentives, including hefty tax breaks, would be enough to compel them to invest their core technology in the local market. Cisco noted that it had chosen to forego filing for the high-end new enterprise certification,

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which would require the company to share its core technology, and was giving up a major tax rebate as a result.

¶6. (SBU) Industry representatives were similarly wary of recent developments in indigenous innovation policy. Corning Inc.'s representative Ken Chan noted that indigenous innovation policies were beginning to "guide" investment decisions, even if they were not yet "determining" factors in whether to invest in China. Other participants noted that China's promotion of indigenous innovation was forcing their companies to do additional rounds of analysis of the regulatory environment before investing. Still other companies expressed concern over "second order" effects of China's indigenous innovation policies, including preference for domestic firms in government procurement, standards requirements, and onerous licensing terms for foreign companies.

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Litigation: Is the Juice Worth the Squeeze?

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¶7. (SBU) Roundtable participants were divided over the benefits of pursuing civil litigation in China. Jay Hoenig of Hill and Associates, a security and risk management consultancy, said Shanghai is entering into a new period in which enforcement and litigation outcomes are increasingly predictable and encouraged foreign companies to take greater advantage of civil litigation. He stated it was hard to make the argument that China's civil system was ineffectual if litigants did not pursue all of the legal remedies available to them. A pharmaceutical industry

representative echoed these comments, noting that in his experience, "99 percent of civil cases involved Chinese rights holders suing other Chinese nationals while only 1 percent of civil cases involved foreign companies suing Chinese defendants. Yet the vast majority of the complaints about the civil system tend to be from foreign rights holders."

18. (SBU) Tao Taodi of Cisco Systems offered a differing view, claiming Cisco was a textbook case of how litigation in China can backfire and hurt a company's long-term interests. She noted Cisco now had regrets over having sued state-owned telecommunications giant Huawei in 2003 because, during the suit, Cisco was portrayed by the Chinese media as a bullying multi-national corporation trying to crush a local competitor. Ultimately, Tao argued, the damage to Cisco's reputation in China outweighed any benefit achieved through the lawsuit. Tao recommended that other companies seriously consider the long-term implications of pursuing civil actions in China. Motion Picture Association (MPA) representative William Feng agreed, noting that MPA had been reluctant to engage in wide-spread litigation against online pirates for fear of drawing the wrath of Chinese netizens, many of whom currently enjoy access to free content. GM's Ken Wong cited the GM Daewoo vs. Chery case as an example of how refraining from litigation may, in some instances, be more useful than pursuing a civil case in China. In 2005, GM Daewoo initiated a law suit against Chinese car manufacturer Chery Automobile Company for copying the design of its Matiz model. GM, however, ultimately decided to settle with Chery after much internal deliberation. As a result, GM Daewoo was seen as a good corporate citizen by the Chinese government and still retains a positive reputation with the Chinese public.

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Copyright Enforcement Weak Link in Shanghai
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19. (SBU) Motion Picture Association (MPA) stressed that it had been effectively shut out of the China market but expressed hope that with the 2010 World Expo Shanghai would do a better job of cracking down on retail piracy. MPA singled out a lack of cooperation between the Shanghai Municipal Public Security Bureau and the Copyright Bureau as a key concern. MPA also hoped that Shanghai would consider adopting tactics similar to those used by Chaoyang district in Beijing to prosecute more infringers. (Note: In March 2006, Beijing City and Chaoyang District Administrations for Industry and Commerce issued notices establishing a "trademark authorization system," which obligates landlords to check the sources of their goods and verify legal authorization from rights holders. End Note.)

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Pharmaceutical Industry Concerns
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10. (SBU) Shanghai-based pharmaceutical companies cited data protection as their top concern and called on the USG to raise the profile of this issue in negotiations with the Chinese Government. According to the representatives' estimates, U.S. pharmaceutical manufacturers lost \$1bn in China last year to

piracy and counterfeiting. The representatives claimed IP infringement would disappear overnight if the State Food and Drug Administration (SFDA) had the political will to enforce China's existing laws. The pharmaceutical industry representative also cited lack of action on SFDA's 2005 regulation on patent linkage as another key concern and asked the USG to urge SFDA to stop issuing licenses to Chinese companies who do not own patents for their pharmaceutical products. He stressed that, in order to gain the maximum amount of traction with SFDA, it was critical to frame these issues in an economic context, highlighting how better data protection will lead to more indigenous innovation and more jobs.

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Recommendations for Continued Outreach

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¶11. (SBU) Participants were enthusiastic about the Ambassador's proposal to locate and designate "model IP cities," which might tap into a "culture of competition" between Chinese cities spurring one another to raise their standard of IP protection and enforcement. They also endorsed re-invigorating the U.S. Ambassador's IPR roundtable and supported the idea of inviting domestic Chinese companies to participate in future roundtables, which, they said, would help make a more compelling case that IP protection and enforcement helps both foreign and domestic

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companies. Pharmaceutical industry representatives noted in particular that East China has several innovative domestic pharmaceutical companies, which could be enlisted in this effort. GM's Ken Wong said that Geely Automotive, a large privately owned firm in Zhejiang Province, might also be a willing participant, given Geely's efforts to break into the U.S. market. When asked whether Chinese companies might be afraid of being perceived as being too close to U.S. companies and the USG, Cisco's Tao Taodi said that those perceptions would ultimately depend on who was organizing the event. Chinese firms would most likely be more comfortable with some Chinese Government involvement. GM's Wong proposed one possible solution would be for the USG to partner with a local government agency and jointly sponsor the program.

¶12. (SBU) Other industry representatives noted their success in working directly with local governments to establish public-private partnerships, and cited Microsoft's R&D center and affiliation with local universities, as an example. Cisco Systems is also working with local governments and recently signed an MOU with the government of Chongqing, featuring a section encouraging greater IPR protection.

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Comment:

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¶13. (SBU) The extremely frank observations by the U.S. industry representatives -- particularly with respect to their own interests in dealing with the China's tricky IPR environment -- impressed the USG participants in the roundtable. Overall, the approach favored by industry tended toward accentuating the positive, i.e. looking for ways to convince the Chinese authorities at all levels that robust enforcement of intellectual property protection serves China's long-term

interests. Notably, none of the industry participants indicated they would be leaving the China market despite their ongoing IPR problems.

¶14. (U)Embassy Beijing and USTR have cleared on this cable.
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